

*Example 1.* The taxpayer, who was in the business of building houses, purchased an undeveloped lot of land for \$500 and built a house thereon at a cost of \$10,000. Subsequently, he transferred the right to hold the lot improved by the house for a consideration of \$12,000, and an annual ground rent for such property of \$120 which was redeemable for a redemption price of \$2,000. The taxpayer reported a \$2,000 gain on the transfer, treating the amount realized as \$12,000 and his cost allocable to the interest transferred as \$10,000. Since the builder did not take the redeemable ground rent into account in computing gain on the transfer, his basis for such ground rent is \$500 (the cost of the land not offset against the consideration received for the transfer). Thus, if he subsequently sells the redeemable ground rent (or if it is redeemed from him) for \$2,000, he has no gain of \$1,500 in the year of sale (or redemption).

*Example 2.* Assume the same facts as in Example 1 except that the builder reported a gain of \$3,500 on the transfer, treating the amount realized as \$14,000 (\$12,000 cash plus \$2,000 for the redeemable ground rent) and his costs as \$10,500 (\$10,000 for the house and \$500 for the lot). Since the taxpayer took the entire amount of the redeemable ground rent into account in computing his gain, his basis for such ground rent is \$2,000. Thus, if he subsequently sells the redeemable ground rent (or if it is redeemed from him) for \$2,000, he has no gain or loss on the transaction.

*Example 3.* Assume the same facts as in Example 1 except that the builder reported a gain of \$3,000 on the transfer. He computed this gain by treating the amount realized as \$12,000 but treating his cost allocable to the interest transferred as \$12,000/\$14,000ths of his total \$10,500 cost, or \$9,000. Since the builder still has remaining \$1,500 of unallocated cost, his basis for the redeemable ground rent is \$1,500. Thus, if he subsequently sells the redeemable ground rent (or if it is redeemed from him) for \$2,000, he has a gain of \$500 in the year of sale (or redemption).

[T.D. 6821, 30 FR 6217, May 4, 1965]

**§ 1.1059(e)-1 Non-pro rata redemptions.**

(a) *In general.* Section 1059(d)(6) (exception where stock held during entire existence of corporation) and section 1059(e)(2) (qualifying dividends) do not apply to any distribution treated as an extraordinary dividend under section 1059(e)(1). For example, if a redemption of stock is not pro rata as to all shareholders, any amount treated as a dividend under section 301 is treated as an extraordinary dividend regardless of

whether the dividend is a qualifying dividend.

(b) *Reorganizations.* For purposes of section 1059(e)(1), any exchange under section 356 is treated as a redemption and, to the extent any amount is treated as a dividend under section 356(a)(2), it is treated as a dividend under section 301.

(c) *Effective date.* This section applies to distributions announced (within the meaning of section 1059(d)(5)) on or after June 17, 1996.

[T.D. 8724, 62 FR 38028, July 16, 1997]

**§ 1.1059A-1 Limitation on taxpayer's basis or inventory cost in property imported from related persons.**

(a) *General rule.* In the case of property imported into the United States in a transaction (directly or indirectly) by a controlled taxpayer from another member of a controlled group of taxpayers, except for the adjustments permitted by paragraph (c) (2) of this section, the amount of any costs taken into account in computing the basis or inventory cost of the property by the purchasing U.S. taxpayer and which costs are also taken into account in computing the valuation of the property for customs purposes may not, for purposes of the basis or inventory cost, be greater than the amount of the costs used in computing the customs value. For purposes of this section, the terms *controlled taxpayer* and *group of controlled taxpayers* shall have the meaning set forth in § 1.482-1(a).

(b) *Definitions*—(1) *Import.* For purposes of section 1059A and this section only, the term *import* means the filing of the entry documentation required by the U.S. Customs Service to secure the release of imported merchandise from custody of the U.S. Customs Service.

(2) *Indirectly.* For purposes of this section, *indirectly* refers to a transaction between a controlled taxpayer and another member of the controlled group whereby property is imported through a person acting as an agent of, or otherwise on behalf of, either or both related persons, or as a middleman or conduit for transfer of the property between a controlled taxpayer and another member of the controlled group. In the case of the importation of property indirectly, an adjustment